

Testimony of

Elizabeth A. Duke

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Committee on Financial Services

United States House of Representatives

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Mr. Chairman, I am Betsy Duke, an executive vice president of Wachovia Bank and Chairman of the American Bankers Association (ABA). ABA, on behalf of the more than two million men and women who work in the nation's banks, brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks – makes ABA the largest banking trade association in the country.

I want to thank you, Mr. Chairman, for having this hearing. Today, as in past hearings of this committee, we want to emphasize that bankers and many in the real estate industry are much more closely aligned on the issue of real estate brokerage than the rhetoric on this issue might suggest. We all believe that customers deserve to have the best possible service, regardless of what company provides it. We all want customers to have many choices so they can seek out the agent or company with whom they want to do business. And we all believe that the provision of any financial service should be done in a safe and sound manner – including adhering to all state licensing, qualification, sales practices, and continuing education requirements.

Of course, there are differences that distinguish our respective positions on the matter of permitting banks to engage in real estate brokerage and management services directly. We believe the issue boils down to two fundamental issues: (1) the benefits of banks' involvement in real estate, and (2) the appropriate process for determining in which activities banks can be involved.

We believe there is great merit in bank involvement. If nationally-chartered institutions could offer real estate brokerage and management services, consumers would have more choices of real estate firms when buying or selling a home. Real estate agents would have more choices of

potential employers. And real estate companies would have more choices of firms to partner with that could provide new sources of capital and technology. By prohibiting bank involvement, consumers, real estate agents and real estate companies have *fewer* choices.

We believe a competitive market is the best way to provide quality real estate brokerage and management services. Increased competition in a market economy benefits consumers by encouraging innovation, increasing efficiency, and lowering prices. This bedrock principle is true in every segment of our economy. Banks are seeking the ability to enter the real estate brokerage industry and, in doing so, to increase competition to the benefit of home buyers and sellers. Naturally, this added competition would affect Realtors. No business is, or should be, immune from competition. Banks engaging in real estate services would be competing with one another also, just as they do now for consumers' checking accounts and other banking needs. We are not talking about some monolithic, imaginary bank entity that would blot out the market to the detriment of local consumers. We are discussing the ability of thousands of regional and community banks, which are already at work in their local communities, to invigorate the real estate brokerage market with new choices and products at competitive prices. To listen to the National Association of Realtors (NAR), keeping banks out of the real estate brokerage industry is all about protecting customers. In reality, their campaign has been about protecting themselves from the stimulating effects of competition.

This issue of open and fair competition is not new – in fact, it has been debated in this legislative body for many years. In 1999, Congress took an historic step to modernize the regulation of the financial services sector by passing the Gramm-Leach-Bliley Act (GLB Act). In the 20 years of debate on the issues covered by the Act, Congress often found itself in the middle of arguments between financial services industries about who should be able to do what. The result was gridlock and an out-of-date financial system that did not reflect changes in consumer needs or in the use of technology.

The GLB Act created the necessary and appropriate framework for determining what services banks should be able to provide. To be sure that the pro-competitive goals of the GLB Act

continued to be met in a dynamic marketplace, Congress established a flexible, yet conservative regulatory process that would permit the financial industry to offer new services without the need for further legislation. This regulatory system gives the Federal Reserve and Treasury the *flexibility and responsibility* to determine what activities should be approved, including considering what is necessary to permit financial holding companies and national bank subsidiaries to “compete effectively with any company seeking to provide financial services in the U.S.” This authority is consistent with the Federal Reserve’s and Treasury’s role to ensure efficient, safe, and competitive financial markets.

Those involved in the debate over the many years that led up to the GLB Act should not have been surprised to see the current proposal to allow banks to offer real estate brokerage and management services. Over a decade ago, ABA and NAR negotiated rules under which banks would enter the real estate brokerage business. This negotiation was in the context of an early version of the GLB Act which was much more restrictive than the criteria enacted in 1999. Thus, over ten years ago, NAR recognized that even a more restrictive version of financial modernization could be interpreted as permitting banking companies to offer real estate brokerage services. Furthermore, in 1995, NAR testified on yet another more restrictive forerunner of the GLB Act before the House Banking Committee. In that testimony, NAR stated unequivocally that the language must be clarified to exclude real estate brokerage and management. *It was not clarified then, nor was it clarified in the GLB Act.* Certainly NAR had every opportunity to raise the issue with Congress in 1999 and either chose not to or did so without success.

The GLB Act is a solid, well thought out piece of legislation. It promotes competition and safety and soundness, and enables Congress to avoid becoming embroiled in every competitive issue. NAR’s position, embodied in H.R. 111, is anti-competitive and anachronistic. It would reverse the most important long-term provision in the GLB Act and would put Congress back in as referee for future competitive disputes. Having worked so hard to develop a mechanism to continually keep our financial system up-to-date, Congress should not reverse itself to protect NAR from competition. The system established in the GLB Act should be allowed to work and H.R. 111 should not be enacted. Moreover, Congress should not be asked to choose between banks and

Realtors. This is a choice for consumers to make based on their own unique set of needs and preferences.

With housing prices at an all-time high – costing homebuyers and sellers tens of thousands of dollars with each real estate transaction – there is no better time to allow greater competition into the marketplace. Simply put, banking institutions should be allowed to offer real estate brokerage and management services for three key reasons:

- ***It's good for consumers*** – It means more choices, better service, competitive prices and greater convenience. Competition stimulates innovation and encourages effective uses of technology to better serve consumers.
- ***It's only fair*** – Since real estate firms offer banking and insurance services, it's only fair that banking institutions be allowed to provide real estate services. This is what the Gramm-Leach-Bliley Act is all about – promoting free and fair competition by leveling the playing field.
- ***It's safe*** – All consumer protections, *including all state licensing, qualification, sales practices, and continuing education requirements that apply to Realtors, plus strict privacy laws and anti-tying rules*, would apply to bank-affiliated real estate agents. And because brokerage and management are agency activities, they pose no risk to the bank.

I will discuss these points in detail in the remainder of my statement.

I. Competition Benefits Consumers

The benefits of competition are well known. In a free market, businesses choose to offer new products if they believe they can provide better services at competitive prices. Obviously, not all banking organizations will choose to offer real estate services, but those that do will enter the market because they believe they can meet or beat the competition. Increasing the number of providers raises the bar for all the participants, forcing improvements in efficiency, pricing and service levels – *all to the benefit of homebuyers and sellers.*

Allowing all banking institutions to provide real estate services expands the choices for everyone: consumers, real estate agents and real estate companies.

More Choices for Consumers

More players in the real estate business mean more and better products for consumers. In any competitive market, new participants bring new, creative ideas to the market – all designed to provide better service and greater convenience, at reasonable prices. In fact, businesses can only be successful in new markets by providing services that meet the needs of customers. Free competition among a wide variety of providers is the cornerstone of our economic system.

More Choices for Real Estate Agents

Real estate agents pride themselves on being independent contractors, choosing the best companies to work for. If there are more companies to choose from, agents' employment opportunities will be much broader. Banks will only be able to attract good agents by offering competitive commissions and other incentive-based compensation packages. And because the real estate business requires expertise, licensing, and other requirements, banks would seek out experienced real estate agents.

More Choices for Real Estate Companies

Forward-looking businesses are always looking for opportunities to improve their franchise value – strengthening, expanding, merging, or even selling their business. Allowing banking institutions to engage in real estate brokerage and management services gives real estate companies more options for bringing additional capital and technology to the table, through joint ventures, for example. Banking institutions also represent potential buyers if agencies choose to sell their businesses. Indeed, in some communities, partnering with the local bank may be the only way for the local real estate broker to compete with the growing national chains.

The Real Estate Services Providers Council (RESPRO) also supports bank entry into the real estate brokerage business. RESPRO is a national non-profit trade association comprised of real estate broker-owners, real estate franchisers, mortgage lenders/brokers, and other settlement service providers throughout North America.

Simply put, ABA believes a competitive market is the best way to provide quality real estate brokerage and management services – more competition means more choices. Circumventing the regulatory process begun by the Federal Reserve and Treasury in 2000 reduces choices: consumers would have fewer choices of whom to do business with, agents would have fewer choices of whom to work for, and businesses would have fewer choices for joint marketing, fewer potential merger partners, and fewer potential buyers.

Technology & Competition Should Lead to Greater Efficiencies

Competition is critical to enhancing efficiency. The real estate brokerage market has not benefited from the efficiency gains typical of other businesses that are so information intensive. As Steve BelBianco and Michael Tavilla noted in their study *The State of eCommerce 2002: Beyond the Bubble, Beware the Barriers*: “Few industries stand to gain as much information, convenience, and efficiency from technology as the buying and selling of homes. Yet this industry has been slow to

adopt Internet and eCommerce technologies and business models, and has erected barriers to prevent innovation and competition – even from within industry ranks.”

Technology has reduced costs. The Internet has driven housing search and property information costs down considerably. More individuals are researching available properties for sale. Buyers can themselves gather key bits of information about property location, flood history, contract status, room dimensions, etc. NAR’s own surveys bear this out, finding that Internet buyers spend more than twice as much time gathering information prior to contacting an agent. At the same time, they moved much more quickly once they began to work with an agent, spending much less time with their agent and previewing far fewer homes compared to pre-Internet buyers. Moreover, buyers who used the Internet spent on average two weeks with their real estate agent and looked at approximately seven homes. Pre-Internet buyers spent approximately six weeks with their agents and looked at approximately 15 homes before purchasing.

In January 2004, the California Association of Realtors conducted its 5th Annual “Internet Versus Traditional Buyers Survey” exploring the home-buying process. For the first time in the history of this survey, more than half of the respondents were classified as Internet buyers, defined as those who used the Internet as a significant part of the home buying process. Internet buyers as a percentage of all buyers rose from 45 percent in 2003 to 56 percent in 2004, while the percentage identified as traditional buyers fell from 55 percent to 44 percent. This trend is expected to continue.

With individuals assuming more of the responsibility to gather and assess information, less time and effort is required by real estate agents in assessing market conditions (for sellers) and in identifying and showing houses. The cost of an agent’s service, therefore, should go down reflecting this shift in burden.

Technology and efficiency improves the delivery of real estate services. Professors Natalya Delcours (Mitchell College) and Norm Miller (University of Cincinnati) found that sales commissions are abnormally high in the United States compared to other countries where fewer barriers to competition exist. Out of the 31 countries studied, only four – *Russia, Belarus, China and Mexico* – had commission rates higher than those in the United States (see Table 1). Not surprisingly, the study found that commission rates are lower when the “information within the market is more efficient, open, and reliable.”¹ Conversely, rates are higher in countries where information is often costly and unreliable in less developed countries – something not characteristic of developed countries with competitive markets.

The authors state: “It appears that commission rates in the U.S. are abnormally high for a country as efficient as we presumed and as price competitive as we would like it to be.”² Moreover, “It is hard to argue that non-U.S. countries have more efficient communication technology, real estate public information or record access that would lead to lower commission rates.”³

Table 1 List of Countries by Commission Fees	
Country	Real Estate Commission Fee (mode)
Hong Kong	1%
Netherlands, Singapore, United Kingdom	2%
Belgium, Denmark, Italy, Japan, Malaysia, Norway	3%
Greece, Ireland, Israel, Thailand	4%
Germany	4.5%
Australia, Brazil, Canada, Caribbean, Finland, Indonesia, Philippines, Spain, Sweden	5%
Argentina, United States	6%
China, Mexico	7.5%
Belarus, Russia	10%

¹ Natalya Delcours and Norm G. Miller, International Residential Real Estate Brokerage Fees and Implications for the U.S. Brokerage Industry, International Real Estate Review, 2002, Vol. 5, No. 1: page 24.

² Ibid., page 28

³ Ibid., page 14

Simply put, competition drives efficiency, innovation and ultimately the cost of services to customers. Putting in place a system that enhances competition – as the GLB Act clearly did – is the best way to provide value for customers at the best price possible.

II. Gramm-Leach-Bliley Act: Flexibility to Adapt to Evolving Market

The GLB Act established a framework for keeping our financial system up to date. After working on this for the last 20 years, Congress recognized the need for flexibility in the face of a rapidly evolving financial landscape. As Senator Phil Gramm said at the signing ceremony for this Act: “The world changes, and Congress and the laws have to change with it....We have learned that we promote economic growth and we promote stability by having competition and freedom.”

Providing the same opportunities under the same rules and regulations is a key to promoting free and fair competition. In today’s real estate market, it is commonplace for real estate companies, securities firms and insurance companies to provide end-to-end services, including brokerage, mortgages, and insurance. We believe this combination of services is good for consumers. Yet not all financial service players have equal ability to offer these options. GLB Act was designed to address these inequalities.

To examine this in detail, this section looks at three key issues:

- The marketplace reality that real estate firms are already providing banking and other financial services;
- The flexibility established in the GLB Act to correct disparity in the provision of financial services among providers and thereby promote free and fair competition; and,
- The changing real estate and financial marketplace that demands a flexible regulatory approach to address inequities that exist today and may exist in the future.

Marketplace Reality: Real Estate Firms Already Provide Banking Services

Combining real estate brokerage and banking services is not a new or unusual activity. Securities firms, insurance companies, credit unions, savings associations and, in more than half the states, state-chartered banks can offer real estate services.⁴ Ironically, in arguing against banks' entry into the real estate brokerage industry, NAR objects to the very combinations that their members have undertaken – offering brokerage, mortgage banking, and, often, insurance under one roof.

Take, for example, two of the biggest real estate companies in the Washington, D.C. area – Weichert and Long & Foster. Both offer the full range of financial services. Weichert's full range financial service program is called, "Weichert Gold Services" and the slogan is "One Stop, Many Solutions." Long & Foster's program is called, "The Real Edge in Homeownership."

These examples show the importance real estate companies – and their customers – place on having the option to combine real estate brokerage, mortgage and insurance services. These combinations of services are good for consumers, providing them with lower costs, greater convenience and more service options. ABA believes that all insured depositories should have the same opportunities to meet the needs of our customers. In fact, according to NAR's own surveys and others', not only is one-stop shopping viewed very positively by homebuyers, but banks, mortgage companies and real estate companies are all viewed *equally* as appropriate providers of these services.⁵

⁴ See attachment developed by the Conference of State Bank Supervisors (CSBS) for a listing of the authorities for each state. Regarding credit unions, in November 1999, The National Credit Union Administration granted federal credit unions the pre-approved authority to offer real estate brokerage services through their credit union service organizations (See 12 Code of Federal Regulations Part 712.5(p)). Since then, numerous credit unions have started to offer real estate brokerage services to complement their mortgage lending operations. For example, Westconsin Credit Union advertises that it now offers full-service real estate services to western Wisconsin at a lower listing fee through Westconsin Realty LLC, a credit union service organization. Credit unions use discount brokers also to cross sell its mortgage products as a one stop solution.

In May 2005, a dozen Pennsylvania credit unions formed a consortium with the Pennsylvania Credit Union Association to create a real estate brokerage, CU Realty Pennsylvania.

⁵ Murray Consulting, *Consumer Perspectives on Realty-Based One-Stop Shopping*, April 2002

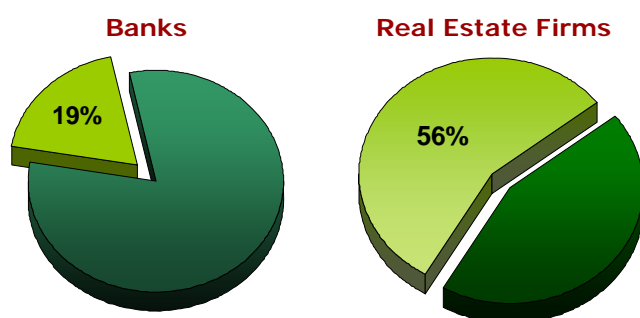
If many real estate and other financial firms already combine real estate services and other financial products, there is no reason to deny any banking organization the same opportunities to provide these products to their customers. Not only is it true that real estate firms already provide end-to-end services, it is also true that the largest real estate companies have been increasing their domination over the market.

Chart 1

It is not surprising that the real estate industry is increasingly concentrated (see Chart 1). In fact, the top *three* firms⁶ in the brokerage business control 56 percent of the market. By comparison, the top 50 banks have 56 percent of the banking market. Cendant Corporation accounts for one out of every three real estate agents and alone has a 34 percent market share of existing home sales.

The Real Estate Industry is Much More Concentrated than the Banking Industry

■ 2004 Market Share of Top Three Firms



And because consolidation within the real estate industry is occurring at breakneck speed, small realty companies are far more likely to be bought up by one of the major real estate firms than by a bank. Many real estate brokers have told ABA that they would welcome approval of the proposal because it would provide a potential local partner to help them compete with the large national chains. In fact, the local bank can help the small firm, through joint ventures and the provision of capital, to compete with the large national real estate firms.

With a more concentrated market than banking, it is ironic that NAR claims only large banks are interested in real estate powers and will come to dominate the market. In my opening remarks I made the point that this is an issue for banks of all sizes, not just large banks. Nearly 40 percent of all banks – 3,380 institutions – have fewer than 25 employees. These are small businesses by any definition and they would like the opportunity to broaden the financial products they can

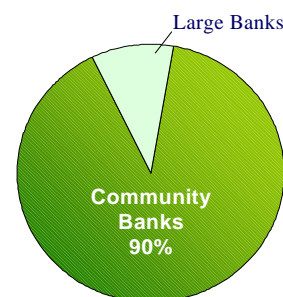
⁶ Cendant, RE/MAX, and Prudential Real Estate

offer their customers and to compete with real estate firms offering loans and homeowners insurance.

It is also a misconception that all national banks are large (see Chart 2). In fact, ninety percent of national banks are community banks. Moreover, it appears that half of the 10 largest banking firms already have the legal authority to engage in real estate activities. There certainly has been no market disruption from the fact that well over half of the insured depository institutions in this country have the ability to offer real estate brokerage and management services today.

Chart 2

Ninety Percent of National Banks are Community Banks*



* Defined as banks with less than \$1 billion in assets

Banks that already offer real estate services through the trust department frequently find themselves having to explain to customers that the bank cannot help them with these services outside the trust relationship. These customers do not understand why the bank is unable to do so. Authority to offer real estate services by these banking organizations would bridge this unnecessary gap.

The GLB Act Was Designed to Allow Flexibility to Adjust to the Marketplace

In the years immediately preceding passage of the GLB Act, Congress recognized that the statutory standard for regulatory approval of new activities for bank holding companies — the “closely related to banking” standard — was woefully inadequate in an economy transformed by technological progress. Thus, Congress agreed to a new, considerably broader, standard to enable banks and bank holding companies to remain competitive no matter in what direction financial services evolved. That new standard — activities that are financial in nature or incidental to a financial activity — was intended to provide the flexibility Congress knew would be necessary. Those activities may be conducted only in financial holding companies (FHC) or financial

subsidiaries meeting certain safety and soundness and community needs standards enumerated in the statute.

Congress did not give the Federal Reserve and the Treasury unfettered discretion to make the determination that an activity is appropriate for approval. The GLB Act specifically sets forth certain traditional banking activities that Congress knew were clearly financial in nature.

In addition to these currently-recognized activities, the Act authorizes activities that the Federal Reserve and Treasury determine, by regulation or order, to be “financial in nature or incidental to such financial activity.” This authority to permit new financial activities is considerably broader than the Federal Reserve’s comparable authority before the GLB Act was enacted, which had only extended to a new activity that was “so closely related to banking as to be a proper incident thereto.”

One specific aspect of this new authority is that the Federal Reserve is directed to define the extent to which three types of activities are “financial in nature”: (1) lending, exchanging, and engaging in certain other transactions with financial assets other than money or securities; (2) providing any device or instrumentality for transferring money or other financial assets; or (3) arranging, effecting, or facilitating financial transactions for the account of third parties. ABA believes the proposed real estate activities qualify under the first and third statutory categories. For example, real estate brokerage is generally the business of negotiating a contract for the purchase, sale, exchange, lease, or rental of real estate – which we believe is a financial asset – for others.

That real estate is a financial asset cannot be questioned. It is clearly the most important financial transaction for the great majority of people. It is not only the largest monetary transaction in which most people engage, but also the mechanism through which they accumulate a great portion of their wealth over time. In many cases, real estate also serves as a means of wealth creation through increases in value and by providing real economic benefits through the tax structure. In addition, real estate serves as the underpinning for hundreds of billions of dollars in securities due to the securitization of home mortgages and other real estate loans not only for the private sector banking industry, but also for numerous government-sponsored entities, such as secondary market giants Fannie Mae and Freddie Mac.

The Federal Reserve and Treasury, in their request for public comment, noted that many of the essential aspects of real estate brokerage are already permissible under national bank “finder” authority. The regulators already authorize financial holding companies, as well as national banks and their subsidiaries, to act as finders in bringing together buyers and sellers for financial or non-financial transactions. Permissible finder activities include “identifying potential parties, making inquiries as to interest, introducing or arranging meetings of interested parties, and otherwise bringing parties together for a transaction...”⁷ This description of finders authority is the essence of every real estate transaction.

Apart from their authority with respect to these three specified activities, the Federal Reserve and Treasury have broad discretion to determine that other types of activities are “financial in nature or incidental to such activity.”

In making such a determination, the regulators are directed to consider a number of factors. Among the specific factors to be considered are:

- Changes or reasonably expected changes in the marketplace in which financial holding companies compete or the technology for delivering financial services; and
- Whether the proposed activity is necessary or appropriate to allow a financial holding company to –
 - Compete effectively with any company seeking to provide financial services;
 - Efficiently deliver information and services that are financial in nature through the use of technology, including applications involving systems for data transmission or financial transactions; and

⁷ 12 CFR 7.1002.

- Offer customers any available or emerging technological means for using financial services or for the document imaging of data.

The GLB Act standard is a significant expansion of the Federal Reserve and Treasury's capacity to consider the competitive realities of our nation's financial marketplace when determining permissible activities for financial holding companies and financial subsidiaries. It is our contention that the marketplace, and the technology associated with it, in the case of real estate brokerage and property management, have already changed and will continue to change dramatically in ways that significantly impact the ability of banks to effectively compete with other companies that provide financial services.

Finally, in addition to the newly-authorized financial activities described above, the Act authorizes financial holding companies to engage in certain non-financial activities. Specifically, a financial holding company may engage in a non-financial activity, or acquire a company engaged in a non-financial activity, if the Federal Reserve and Treasury determine by regulation or order that the activity: (1) is complementary to a financial activity; and (2) does not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally.

NAR would have this Committee believe that Congress meant to preclude real estate activities in the GLB Act and that the legislation accomplished that goal. This assertion is simply untrue; we have seen no evidence to back up this unfounded charge. There is absolutely nothing in the legislative history to support this allegation. To the contrary, the plain language of the statute and the legislative history show that the Treasury and Federal Reserve are following the process and using the factors Congress intended.

The GLB Act itself demonstrates Congress's knowledge of this issue in its determination that financial subsidiaries of national banks should be prohibited only from engaging in real estate development activities – the riskier aspect of the business in which the banking organization takes an ownership position. Had Congress intended to prevent banking organizations from engaging in the agency activities of real estate brokerage and real estate management, the Members involved clearly knew how to do so. The fact that Congress chose only to prohibit real estate development underscores the conclusion that Congress did not intend to restrict agency activities.

Certainly NAR had every opportunity to raise the issue with Congress in 1999 and either chose not to or did so without success. Rather, NAR's simplistic argument is that the proposal involves "commerce" and is, therefore, beyond the scope of the GLB Act. However, the issue is not at all that simple. The language of the relevant provisions of the GLB Act does not prohibit commercial activities; rather they set out specific criteria to determine permissible activities. The authors clearly recognized that there was no exact or permanent line to define services that should be permissible. That is why they left the determination of whether or not a given activity is financial in nature or incidental to a financial activity to the Federal Reserve and Treasury, and why they developed the specific criteria that are in the statute. To reiterate, if Congress had wanted to make such a determination to exclude the proposed activities, it would have explicitly done so – as it did with real estate development.

It is worth noting, since NAR has raised the specter of banking and commerce, that the Federal Reserve has, for many years, been the primary opponent of breaching the wall between banking and commerce. Based on this record, one would certainly expect the Federal Reserve to look very closely at any question relating to commercial activities.

As the next section demonstrates, the real estate market is changing rapidly and with each passing day, the competitive imbalances increase.

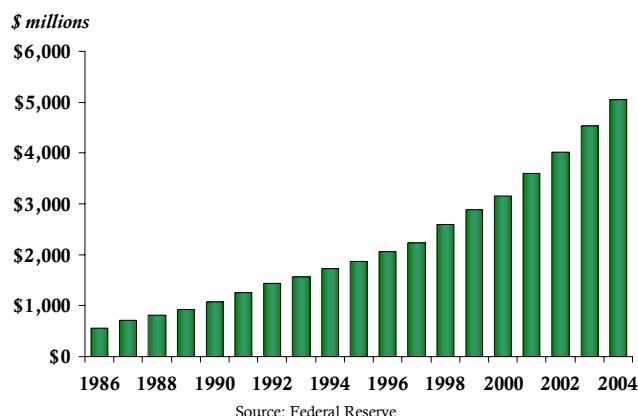
Changing Real Estate & Financial Market Requires a Flexible Regulatory Approach

As noted above, the GLB Act requires that the regulators consider competitive factors and technological innovations when determining whether activities are financial in nature. A particularly applicable statutory phrase to focus on in this context is whether the activity is "appropriate" to allow institutions to "compete effectively with any company seeking to provide financial services in the U.S." Other types of insured depository institutions have the authority to provide – and are providing – real estate brokerage and management services. We have already demonstrated that real estate brokerage firms are providing financial services throughout the U.S. Clearly, the fact that real estate brokerage firms are offering mortgages and other financial services must be part of the

regulatory consideration. Competitive imbalances like this are the very thing that Congress sought to correct when it enacted the GLB Act, and we believe that the use of the flexibility granted to the regulators under Section 103 (a) is clearly justified in the case of real estate brokerage and management authority for banking organizations.

Technological innovations have also had a dramatic impact on real estate markets. One major change is the development of the secondary market for mortgage loans and the efficient process that bundles individual home loans into highly liquid, globally-traded securities (see Chart 3).

Mortgage Backed Securities Outstanding



The increasing importance of the secondary market has facilitated the rapid growth of mortgage lending outside traditional banking and savings institutions. In fact, securitization has significantly changed the very nature of mortgage funding, enabling real estate firms to establish their own mortgage companies and to offer end-to-end real estate transactions – helping a buyer find a home, finance it, and insure it. The result is that traditional deposit-based lenders – banks and thrifts – are often bypassed completely. These are exactly the kinds of technological changes the GLB Act authorized the Treasury and the Federal Reserve to address.

The dominance of the secondary market is clear evidence that this form of funding for plain vanilla mortgage loans is generally superior in terms of costs to funding with bank deposits. If banks somehow enjoyed some special benefit from deposits, or deposit insurance (which banks pay for through premiums and extensive regulatory costs), banks would not be selling into the secondary market, and the secondary market would not control an ever-increasing share of the marketplace. No amount of deposit insurance can counteract this fundamental principle of efficient markets. More importantly, access to this secondary market source of funding is available equally to mortgage

and banking organizations, and is clearly why real estate companies increasingly are affiliating with mortgage banking companies.

To summarize this section, the GLB Act recognized that achieving the goal of promoting competition necessarily required regulatory flexibility. Section 103 (a) provides that flexibility by authorizing the Federal Reserve and the Treasury, subject to certain statutory guidelines, to approve additional activities for banking organizations. ABA believes strongly that real estate brokerage and management meet the criteria. Of course, the Federal Reserve and Treasury have not made any determination on this proposal. Regardless of their ultimate decision, the Federal Reserve and Treasury should be allowed to follow the process Congress created in 1999.

III. Consumer Protections and Safety and Soundness Are Maintained

If these banking organizations could offer real estate services, consumers would actually have more protections under the law than they do today. *All rules applicable to real estate brokers, including all state licensing, qualification and sales practices will apply equally to bank-affiliated real estate agents.*

NAR has raised the specter of customers being taken advantage of as a result of conflicts of interest that may potentially arise when a real estate broker is affiliated with a lender. The simple fact is that the exact same potential for such abuse occurs, for example, each time an agent from Century 21, Coldwell Banker, ERA (all of whom are affiliated with Cendant) GMAC, Long & Foster or USAA helps a customer buy or sell a house. The same potential exists when a small realty firm offers loans through a mortgage banking company. And yet, although these integrated real estate organizations, as well as state banks in many states, savings institutions, and credit unions, have been selling real estate and funding mortgages for years, there has been no outcry about these conflicts of interest. Why? — Because the Real Estate Settlement Procedures Act (“RESPA”)⁸ requires realtors affiliated with lenders to disclose that fact to customers before the purchase occurs.

⁸ 12 U.S.C. § 2601 *et seq*

RESPA disclosure,⁹ which must be on a separate piece of paper, must state the relationship between the real estate agent and the lender and provide the estimated charges or range of charges of the lender. It must also notify the customer that he or she is *not* required to use the lender and is free to shop around for a better deal. If the real estate agent requires the use of its affiliated lender, that agent violates the kickback and unearned fee provisions of Section 8 of RESPA. The customer is expected to sign an acknowledgement of the disclosure.

In addition, consumers have even more protections when their real estate agent *is* affiliated with a banking organization. Greater protection results from banks and bank holding companies and their subsidiaries being subject to the anti-tying provisions of the Bank Holding Company Act.¹⁰ These statutory restrictions prohibit banks and their affiliates from conditioning the provision of credit on the purchase of another product or service.

Another false impression put forward by NAR is that somehow bank involvement is contrary to the spirit of the Community Reinvestment Act (CRA). Nothing could be further from the truth. Approval of the proposal would help low income and minority communities. Because banks are subject to CRA, they would have every incentive to use their real estate authorities to enhance their outreach to communities. These banks would have incentives to bring real estate services to areas now shortchanged and could use the combination of real estate and financial services to better serve their low-income and minority communities. Moreover, if the real estate unit were a subsidiary of a national bank, that subsidiary would be covered by CRA.

Bank involvement in real estate brokerage and management services is also consistent with safe and sound banking. First, providing these services will help to diversify the income stream of these institutions and help to improve their financial base. Real estate brokerage and management services are activities where a bank acts only as an agent for a third party, *but does not take an*

⁹ The requirement for affiliated business disclosures is part of the regulations of the Department of Housing and Urban Development that implement RESPA. 24 C.F.R. § 3500.15.

¹⁰ Section 106(b) of the Bank Holding Company Act 12U.S.C. Sec. 1972.

ownership position in the property. By their very nature, agency activities pose very little risk to the safety and soundness of depository institutions.

Second, under the GLB Act, the bank regulators must deem a banking organization to be well-capitalized and well-managed before it can participate in any of the expanded financial activities permitted under the GLB Act, including real estate brokerage and property management. Thus, only financially strong institutions would be authorized to engage in these activities.

Third, banking organizations are also subject to Sections 23A and 23B of the Federal Reserve Act, which limit the amount of credit and other forms of support that a bank could provide to a real estate brokerage affiliate or subsidiary. Such limits ensure that the safety and soundness of the bank will not be negatively impacted by its subsidiaries or affiliates.

Fourth, many banking organizations already have years of experience in providing real estate activities. In fact, the purchase, sale and management of real estate are frequently significant aspects of fiduciary asset management in bank trust departments. Because banks currently have trust personnel who provide real estate brokerage and management services on a daily basis to trust customers, providing the service outside of the trust department would not be a new activity in which banking organizations lack expertise. Thus, no new safety and soundness issues would be raised.

Finally, it is important to note that a precedent already exists for bank involvement in real estate activities. In over half of the states, state banking regulators have the authority (either explicitly, through regulatory interpretations, or through wildcard and parity statutes) to allow state-chartered banking organizations to engage in real estate activities (see the attached state-by-state listing developed by the Conference of State Bank Supervisors). Moreover, savings institutions and credit unions already have brokerage authority.

In 2000, as a result of negotiations between the bank and real estate trade associations in the state, the Michigan Banking Code was revised to permit state banks to “engage directly in or own in whole or in part, a real estate brokerage business.” The new law also stated that a bank cannot tie

the accommodation of credits to utilization of the real estate brokerage agency, nor can the bank prohibit the customer from going to other financial institutions to obtain mortgage credit. Banks owning or engaging in real estate brokerage activities in Michigan must also clearly disclose that fact in writing to anyone applying for credit or pre-qualified credit related to a real estate transaction.

In 2002, Virginia became the 28th state to authorize real estate brokerage for state banks when the General Assembly opened up the realty business to state-chartered banks beginning July 1, 2003. The legislation enacted in Virginia represented a delicate compromise reached by the Virginia Bankers Association and the Virginia Association of Realtors. The legislation authorizes a controlled subsidiary corporation of a state bank to engage in real estate brokerage.

While the specific provisions in Michigan and Virginia may not be appropriate at the federal level, the fact is that the banking and real estate industries in both states were able to reach a compromise that broadened consumer choice while at the same time addressing any possible consumer or safety and soundness concerns. Allowing banks and all FHCs the same rights and privileges should enhance the competition for real estate services.

IV. Conclusion

A fundamental purpose of the GLB Act was to enable banking institutions to compete with other financial services providers, and there is ample evidence demonstrating that banks' real estate competitors are touting the advantages of one-stop home buying services. While we as an industry have always looked at real estate brokerage and management as providing us with more options to compete in the long term, with *each passing day*, real estate firms become more deeply involved in financial services such as mortgage and insurance, and banks cannot effectively compete for this business. And with each passing day, the case for allowing banks to offer real estate services only gets stronger.

As an industry we have grave concerns about the broader effects of this controversy and whether it sets a precedent that could hinder future approvals of new powers under GLB. The Act was designed to keep our financial system up-to-date by delegating those decisions to the Federal

Reserve and Treasury. This goal is being frustrated by efforts to take the case for determining what is appropriate back to Congress, placing Congress in the very role that it delegated to the agencies with the greatest level of expertise to make these decisions based on specific statutory criteria.

H.R. 111 not only frustrates the GLB Act process, it reduces consumer choice. Consumers would have fewer choices of whom to do business with; agents would have fewer choices of whom to work for; and businesses would have fewer choices for joint marketing, fewer potential merger partners, and fewer potential buyers. We believe a competitive market is the best way to provide quality real estate brokerage and management services. Increased competition clearly benefits consumers and the economy. It is a catalyst for innovation, more customer choice, better service, and competitive prices.

In this new, competitive environment, bankers and real estate professionals have much to offer to each other – and to consumers. Real estate professionals could provide the personalized services and experience that is their strength. Independent agents who provide good service today know that they will be competitive with *anyone*, whether the competitor is another independent agent or one affiliated with a bank.

Many real estate companies realize the strengths that both industries bring to the table. Banks around the country could provide needed capital, cross-marketing opportunities, and technology to support the growth of local real estate firms. Real estate firms also realize the severe limitations the NAR-supported bill would impose on their ability to joint market, merge, be acquired, or even to buy a bank.

Not only would consumers benefit from bank involvement in real estate services, but also bank involvement is consistent with safe and sound banking. All consumer protections that apply to independent realtors would apply to bank-affiliated real estate agents – plus bank-affiliated agents would be subject to additional anti-tying regulations. And because brokerage and management are agency activities, they pose no financial risk to the safety and soundness of the banking organization.

More than five years ago, Congress made the decision to leave this type of determination to the regulators – so that they could keep the financial structure up-to-date and keep Congress out of the

middle of competitive disputes. NAR continues to put up obstacles to any modernization, content to keep costs high and competition low. Rather than compete head to head, NAR wants to put Congress back in the uncomfortable position of referee. Congress explicitly gave the Federal Reserve and Treasury the flexibility and authority to make these determinations because they have the expertise to understand the dynamic nature of the financial services marketplace. Those agencies should be allowed to carry out the authority that Congress wisely provided to them.

I thank you, Mr. Chairman, for this opportunity to present the views of the American Bankers Association.